REPORT OF RECOMMENDATIONS

OF

GOVERNOR CARROLL A. CAMPBELL, JR.'S

LEASE REVIEW COMMITTEE

JANUARY 1989

FOREWORD

The unparalleled growth in State government, in the face of unclear interpretations of constitutional debt limitations, and extended waiting periods for constructing State owned offices and other facilities, has spurred the growth of lease and lease/purchase arrangements by the State of South Carolina, and most recently, by its political subdivisions. Leases and lease/purchases, often masquerading as a means of circumventing the constitutional limitations on indebtedness, but which, nevertheless, create debts which must be paid, have gained popularity as quick fix alternatives to building State owned office buildings.

Following a series of inquiries and studies from within government, by citizens and an astute and aggressive news media, Governor Carroll A. Campbell, Jr. formed a Lease Review Committee in October 1988, to respond to this voiced concern over State leasing practices from within and without government.

The general purpose of the Committee was to review the leasing practices, policies and procedures of South Carolina state agencies and recommend to the Governor how they might be improved or augmented.

The diligent work of the Committee, and various members of State government who helped prepare information for review and for meetings, and the various individuals who appeared before the Committee is greatly appreciated. The news media

should also be acknowledged for helping to bring this issue to the forefront.

We intend this to be a constructive report, with hopes we can profit from the past and move ahead, improving on what we have. We view the role of this Committee to be prospective, recommending policy and identifying areas of concern, rather than investigative, delving into the particulars of past lease and lease/purchase arrangements.

The following have served with distinction on the Lease Review Committee:

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Fountain Inn, South Carolina

R. Glenn Hilliard, President
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Special thanks to Katie C. Morgan of the Governor's Office, Division of Finance and Administration, for serving as secretary.

Respectfully Submitted,

John S. Rainey
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EXECUTIVE SUMMARY

It seems appropriate to here first describe what appears to have been an educational process at the Budget and Control Board as lease/purchasing has evolved in South Carolina. This Committee views the State Museum and the Robert Mills Building lease/purchase financing arrangements as the first stage in this evolution. Following the failure of the State to pursue other options, these Tier I lease/purchase arrangements were brought to the State by developers, who, racing the clock to benefit from historic preservation investment tax credits that would expire after December 31, 1984, convinced the State that these were the best financing techniques available to restore these two State owned buildings for historic and office space purposes. The economic benefits of the 25% federal investment tax credit ("ITC") would be passed through to the State by the investors, thus achieving for it indirectly a benefit for which the State was not directly eligible. This Tier I lease/purchase arrangement was "deal driven". The developers had found a way to do a real estate tax deal in the twilight of the tax law prior to the relevant effective date of the repeal provision of the Tax Reform Act of 1984. Without the ITC, neither of these deals would have worked. However, the ITC indirect benefit to the State may not have been enough to offset the interest rates built into the lease payments

necessary to service the investor debt incurred in these two transactions.

Then came the Tier II lease/purchase arrangements under which the State entered into a financing agreement with a developer, similar in all but one critically important feature to the Tier I arrangements. The Tier II arrangements involved the Clemson University Computer Center Project ("Clemson Computer Center") and the South Carolina Adjutant General Building Project ("AG Building"). Here the developer was involved in a transaction with the State where financing was obtained in a tax exempt revenue bond type financing. It appears that the developer may have educated the Budget and Control Board by showing them how tax exempt financing could be used to finance both of these facilities in a lease/purchase transaction. The middleman developer remained after the concept was apparently introduced and explained. However, the result was that a bond issue (called "participation certificates") was used to finance both the Clemson Computer Center and the AG Building with leases assigned to support the retirement of the debt. Both of these leases contain the standard "non-appropriation clause", yet the Clemson Computer Center bond issue is rated AAA/AAA, due to bond insurance, and the AG Building bond issue is rated AA without bond insurance. In both instances it is clear that the financial community did not take seriously the non-appropriation clause. (1)

Finally, came the Tier III lease/purchase arrangements. Apparently, now having been introduced to lease/purchasing by developers in the Tier I arrangements, then educated by the developer in tax exempt financing for the lease/purchase used in the Tier II arrangements, the Budget and Control Board was sufficiently knowledgeable in this technique to pursue it on its own without the middleman developer. It is these Tier III arrangements that must not be confused with Tier I and Tier II arrangements, both of which involve middlemen developers, and the first of which involves more expensive conventional financing.

The Tier III arrangements essentially involve State ownership of the property financed with revenue bond type debt. An instrument called a participation certificate is issued the "bondholder" but in all but name it is a bond. It was this Tier III method of lease/purchase financing that was proposed for the new CCI facility in Lee County. Essentially, a prison authority (e.g. a building authority) was to be established to build and own the prison. No middleman developer would be involved although there may have been a third party who would manage it. The prison authority would put out the building contract for bids under the State's standard low bid process. The prison would be constructed and leased to the appropriate State agency -the Department of Corrections- with the standard "non-appropriations" clause in the lease. The prison authority

would issue tax exempt certificates of participation which would carry coupons at the same rate or approximately the same rate, as a South Carolina Revenue Bond-about 25 basis points above the South Carolina General Obligation Bond ("GO Bond") yield for a comparable maturity. (2) This "revenue bond type financing" would give the State, when coupled with the absence of a middleman, a facility at a cost only slightly more expensive than if it had been financed with GO Bonds.

The Lexington I School District proposed lease/purchase financing of its new school facility would work in this same fashion.

To the extent this Committee's pronouncements on lease/purchase arrangements have "tarred all of them with the same brush" it has been unintentional.

The point the Committee makes with respect to Tier III lease/purchase financing is that it wants to be certain that the Budget and Control Board, and the governing bodies of the State's political subdivisions, recognize it for what it is - debt. It is debt in the eyes of the investor and financial communities as the "non-appropriation" clause is viewed as without substantive effect. It may even be debt in the constitutional sense as South Carolina Supreme Court Justice A. J. Finney concluded in his dissenting view in Caddell v. Lexington County School District No. 1 et al. In any event when the Budget and Control Board and the

governing bodies of the State's political subdivisions are making a determination of how much "debt" can be serviced by the State or its political subdivisions, all obligations that must be paid or repaid-lease, lease/purchase, revenue bond, participation certificates, and GO Bonds-should be included in the total indebtedness. It would be constructive if the news media using its reporting process as an educational tool, made the real components of the State's and its political subdivisions' debt clear to the public. It really is an anachronism to engage in the niceties of distinguishing constitutional debt from other obligations which must be repaid when the financial community views them all as indebtedness.

The Committee finds all lease obligations, including all lease/purchase obligations, to be indebtedness of the State or of any political subdivision thereof which incurs them. The Committee disagrees with the majority opinion of the South Carolina Supreme Court in Cadell vs. Lexington County School District No.1 et al. The Committee believes that lease payment obligations incurred under lease/purchase arrangements by the State, or any of its political subdivisions, should be considered debt for constitutional debt limitation purposes. These obligations are undeniably debt in substance and the financial community views the "non-appropriation" clause contained in the State's leases as meaningless form. Leases and lease/purchase arrangements

create debts that must be repaid. A debt by any other name is a debt. (3)

It is the view of this Committee that if any political subdivision of the State, including any school district or special purpose district, failed to meet its payments under a lease or a lease/purchase arrangement, for whatever reason, it is conceivable that the AAA credit rating of the entire State could be threatened. If political subdivisions of this State choose to circumvent the limitations of their bonded indebtedness, then the Committee recommends that they be required to receive the approval of both houses of the General Assembly prior to entering into any lease/purchase arrangement.

The Committee believes the issue of lease/purchases are in fact to be considered debt should be an issue pursued and resolved by the South Carolina General Assembly. This course of action was suggested by Mr. Justice Finney in his dissent in the Cadell case.

It is clear to the Committee that the cheapest forms of financing available for the State government are from the general revenues collected by the State and from the issuance of its GO Bonds. However, there are certain priorities of the State that need to be met on a current basis and cannot be funded out of revenues or GO Bond proceeds. Once the political decision is made to make these priorities necessities, and to fund them as current requirements, then

the only other sources of revenues that should be available to provide money are revenue bonds and Tier III lease/purchase financing.

The Committee finds that pure leasing and Tier 1 and Tier II lease/purchase arrangements provide significantly less attractive financing alternatives than general obligation bond, revenue bond and Tier III lease/purchase financing arrangements. Therefore, leasing, except through relatively short term and limited purposes leases, and Tier I and II lease/purchases should no longer be acceptable as alternative sources of financing available to provide additional office space for State and agency employees.

It is the conclusion of this Committee that in the last year, if not the last six months, a tremendous advancement in the understanding of State leasing practices has evolved. Due to the public discussion, legislative study and media attention, the State is beginning to realize that leasing office space is more expensive in every instance, with the exception of very short term leases, than if the State were to build and maintain its own buildings.

State ownership of buildings is preferred. The Committee agrees that whenever the possibility and opportunity are available the State should own its own facilities.

The Committee finds the State can build, maintain and operate its own facilities at a lower cost than the private

sector. The cost of money is always less for State government than for the private sector. Also State government receives lower power rates, apparently can negotiate cheaper cleaning and maintenance contracts, and does not pay federal or state income taxes or property taxes, costs built into rates offered by the private sector.

The State can finance the construction of its own facilities cheaper than the private sector due to the availability of tax exempt GO Bonds and revenue bonds and Tier III lease/purchase tax exempt participation certificates, all of which carry a lesser interest rate than any debt financing that can possibly be obtained by a private sector developer.

The Committee recommends the creation of a Central Building Authority to build the much needed office space, the ownership of which creates additional assets for the State. The Central Building Authority would build new buildings and have conveyed to it existing buildings. It would then issue revenue bonds or if Tier III lease/purchasing is used, participation certificates, the principal and interest on which would be paid through rental revenues from leases on buildings leased to the State and its agencies by the Central Building Authority. The interest paid on the revenue bonds and the participation certificates would be exempt from federal income taxes and from South Carolina income taxes if the holder were a South Carolina

resident. The amount of indebtedness that the Central Building Authority could issue would be limited by law.

In the use of revenue bonds or Tier III lease/purchase financing as methods for financing, it is more desirable for the State to create a Central Building Authority than an authority for each project. The economies of scale and the inherent increased effectiveness of administration and control are obvious advantages of a Central Building Authority.

The Committee supports and recommends the approval of an Office of Facilities Administration, ("OFA"), within the Division of General Services. (4) The OFA would be a central clearinghouse for acquisitions of all office and other space, by whatever means, for use by State government. The OFA would be charged with tightening current procedures and developing new procedures to assure that the State's leases are entered into and managed on a business-like basis. The only appeal from the OFA would be to the Budget and Control Board. Any decision made by the Budget and Control Board would be final and binding on all parties. The only remedy thereafter would be to the courts.

The Committee recommends that the Discounted Cash Flow method of financial analysis be used as the method for comparing alternative means of financing State facilities' costs.

The Committee believes legislation should be enacted and enforced that prohibits developers from contacting agency heads with respect to lease or lease/purchase arrangements. All such contacts should be initiated and maintained through the OFA.

With regard to preservation, there is a strong argument to be made that the State should preserve architecturally important and historically significant buildings strictly for the sake of preserving the treasure. The Committee finds the two objectives of seeking office space and preserving buildings to be not necessarily compatible, and a very expensive, if not the most expensive way to develop a building. Considering the economics, the Committee recommends as a general rule the separation of the pursuit of historic preservation and the acquisition of office space.

It is the conclusion of the Committee that South Carolina's attractive seat of government at the state Capitol Complex (the Capitol, Gressette, Dennis, Blatt and Brown buildings) is complete and distinctive enough to memorialize our growing State government. Any further buildings constructed by the State should have as a first priority utilitarian construction. Adjacent land should be available for the future addition of more functional capacity. Inherent in the buildings should be the engineering and architectural capacity for expansion with relative ease to accommodate the rapid rate of government growth. This

desirable course for future development may require that the State look beyond the city limits of Columbia toward a campus type environment within which to construct additional buildings.

The Committee recommends that OFA establish rolling three to five year State and agency space allocation plans, updated annually by OFA, to quantify future State and agency space needs.

In response to the continued growth of State government, which every indicator has predicted will continue, the Committee recommends that those agencies that do not specifically need to be in the Capitol area gradually be relocated to a more functionally appropriate and more economically defensible locations. Agency desires to be located near the Capitol appear, with the exception of such high visibility agencies as the State Development Board, whose image and functions require it, to be based largely on prestige or convenience, rather than agency functions and practicality, and should be strongly discouraged. Otherwise, the almost certain growth of future State government promises that most agencies in the limited space of the Capitol area will be severely fragmented in their expansions which will produce locations and configurations of space inherently designed to assure inefficiency and high costs of operations.

The proposed legislation of Senator McConnell is a mighty step in the right direction, but we have noted in some

instances it does not go far enough. While it does attempt to establish some sort of standardization and create a more open leasing system, THE COMMITTEE RECOGNIZES ONE ASPECT OF THE BILL WHICH MUST GO ONE STEP FURTHER: Requiring ALL lease/purchase agreements of the State and its political subdivisions, including school districts and special purpose districts, to have the prior approval of the GENERAL ASSEMBLY. This extension of the approval process would provide much needed control over the apparent impeding proliferation of lease/purchase arrangements throughout the State. This additional provision to the proposed legislation is critical and urgently needed to prevent substantial and irrevocable harm to the credit rating of the State of South Carolina.

This Committee strongly supports the McConnell legislation in general, and recommends that the regulations to be promulgated thereunder be detailed, precise and have "teeth" with adverse consequences for offenders.

The Committee is in agreement that reforms already underway within the Division of General Services are well conceived steps in the right direction for operating a more businesslike State government, where efficiency, cost control, and short as well as long term planning and forecasting are viewed as critical to serving the needs of a growing South Carolina.

Many of our conclusions, reached independently after much study are similar, if not identical in some cases, to those recommendations of the 1987 Study by the Budget and Control Board and the Joint Bond Review Committee. We feel that the State, through its staff and citizens' committee, having inadvertently done much the same lease study twice, should pay special heed to the advantages of having two reports that confirm many of the same conclusions.

INTRODUCTION

The phenomenal growth of State government since the Second World War has created a demand for space that is unprecedented in modern times.

As late as 1946, virtually all of the State agencies located in the Columbia area were housed in three buildings: the Capitol, the Calhoun Building and the Wade Hampton Building. The post war boom followed by the "federal funds" era expanded services and programs in the public sector, particularly in the area of social services, health and education. To meet the immediate needs for real and personal property, the State spawned a short-lived building boom to accommodate the mushrooming government service sector. In the late sixties plans were beginning to be developed to anticipate and fund the capital needs of State agencies. A plan that had been developed in 1971 to guide the State in building additional facilities was widely discussed but never

acted upon officially. Budget and bonding restrictions, in a recessionary era where competition for limited funds was keen, created an atmosphere of prudence and caution. In 1979, after Governor Riley vetoed a $7 million dollar bonding authority to expand the Department of Social Services headquartered in the designated North Towers area, (Bull Street), a number of State officials in various branches of government took the position that the State could not afford to construct more office buildings, regardless of need.

Though admittedly in hindsight, the irony should be noted. In the well meaning effort to appear fiscally conservative by entering into temporary, and some not so temporary, leasing commitments for various periods of time, the State spent more than it would have had it built office space financed with GO Bonds, or at worst revenue bonds, and built a permanent State owned infrastructure. The appreciation in value over time of this State owned real estate investment would have inured to the benefit of the State and its citizens. The appreciation in value of the buildings leased in whole or in part by the State from private developers during this period has inured to their benefit, thanks in no small part to the State being a steady and credit worthy tenant.

To accommodate the needs of an ever growing government sector, which had spilled out of State owned offices, the staff of the Budget and Control Board had leased commercial

space for needed expansion without a long term plan and in piece meal fashion, resulting in cost inefficiencies. Then, in 1984, South Carolina joined a national movement by entering into lease/purchasing arrangements with the "deal driven" renovations of the historic Mt. Vernon Mill and Robert Mills Building.

With respect to Mt. Vernon Mill, which was donated to the State in 1981, it should be noted that after several years of delays, the South Carolina General Assembly and Budget and Control Board had lost interest in recommending bond financing to provide for its restoration as a State Museum. The price tag had climbed from 15 to 25 million dollars in a very short period. The developer proposed Tier I lease/purchase financing appeared to be the only viable alternative for developing the property without a further and perhaps expensive delay.

More than 6,000 facilities are owned by the State. The demand for office space for government employees has created an aggregate budget of 1,013.6 million of which 513.8 million are capital improvement bond funds.

The Division of General Services reported about 1.5 million square feet of State owned office space as of July, 1988. The replacement cost of these facilities is considered to be about 172.7 million as of 1986. The Citadel's inventory includes 70 facilities with about 1.4 million sq

feet of space with a replacement value of more than 96.7 million.

The Department of Parks, Recreation and Tourism's (PRT) inventory has identified some 2,870 facilities within parks located throughout the State including park ranger's houses, picnic and rental shelters, rest room facilities, parking areas and waste treatment systems.

The Division of General Services reported as of July, 1988 about 3.6 million square feet of leased office space and other space being leased throughout the State from commercial and other sources in 595 lease agreements at a cost of over 26.8 million dollars annually.

Data from General Services indicate that the State government has leased more than 1,250,000 square feet of building space for AT LEAST THE PAST TEN YEARS.

This Committee believes that if State government accepts the proposition that long term leasing is more expensive than owning, and that building owners' equity is just as viable an investment for government as it is for private individuals, then it is the responsibility of the Budget and control Board to make owning as practical and as an efficient an alternative to satisfying the State's needs for space, as quicker, but more costly true leasing and Tier I and Tier II leasing/purchasing.

According to the landmark and generally overlooked Budget and Control Board's and Joint Bond Review Committee's STUDY OF LEASE PURCHASE AND OTHER PRIVATE FUNDING MECHANISMS FOR CAPITAL IMPROVEMENTS (January 1987) - "1987 Study" -, "Most of the real property (land and buildings) and the personal property (equipment) used by the State government is owned by the State government. And, most of it was purchased outright over the years using cash appropriated by the General Assembly from then-current revenue income or from bond proceeds. (Note: The 1987 study indicates the State owns and leases at least 6.0 million square feet of office and other space, of which approximately 2.2 million or 37% is leased space.)

"However, in recent years, private funding mechanisms, including true leases, have been used extensively to provide the land, buildings, and equipment needed in the operation of government...It can be said that the availability and the use of the true lease private funding mechanism is essential to the operation of the State government. However, a compelling case for the use of the lease purchase mechanism cannot be made..." (5) (6)

The decision to lease, rather than buy buildings was a political decision, which on the surface, seemed prudent at the time. Rather than raise taxes to pay for buildings, the state borrowed money and used the debt for general revenue purposes. The constitutional definition of debt at the time

did not specifically include, nor preclude, leases or lease/purchases even though generally accepted accounting principles, as well as the investment community would consider such financial obligations to be indebtedness. (7)

"One of the arguments being advanced is that payments required under lease purchase arguments are not debt in the strict Constitutional limitation sense. One implication of the "not debt" argument is that the cost of such agreements does not count against the debt service/issue limitation and that there should, therefore, be less concern with their use. Because no clear approval process exists on them, lease purchase projects are outside of the priority schedule on the availability of capital improvement bond funds which is the nearest thing the State has to a formal capital budget. The result is that the means of financing winds up giving certain projects a much higher standing in implementation priority than they likely would have gotten otherwise.

"ON THIS POINT, THE STUDY CONCLUDES THAT RESORTING TO METHODS OF FINANCING NEEDED STATE IMPROVEMENTS TO GET AROUND SELF-IMPOSED RULES, LIMITATIONS AND DISCIPLINES IS THE WRONG COURSE TO TAKE. IT CONCLUDES ALSO THAT THAT APPROACH IS TO BE VIEWED WITH HEAVY SKEPTICISM AND THAT THE WISDOM AND ENERGY REQUIRED TO DEVISE ESCAPE ROUTES FROM SELF-IMPOSED RESTRAINTS WOULD BETTER BE INVESTED IN MAKING THE CASE TO CHANGE THE RESTRAINTS WHICH PROMPTED THE LOOK FOR ALTERNATES

IN THE FIRST PLACE. (*) The simple truth is that, regardless of how State financial obligations are classified (and the bond rating houses and accounting standards organizations do consider lease purchase obligations debt), they necessarily must find their place in an appropriations act or in an act which authorizes the issuance of bonds. The issue then, as so often is the case, is what choices are to be made from among virtually unlimited needs/wants and the limited resources available to meet them.....

"Processes for making decisions on the use of private funding mechanism for capital improvements, at worst, do not exist. At best they are inadequate and incomplete...

"Even though, once executed, lease purchase agreements clearly become long-term financial obligations of the State, no general procedure now exists for getting such agreements approved...

"Much the same point can be made about multi-year true lease agreements which also become, as a practical matter, long-term financial obligations when they are executed. The difference with true leases is that, under existing law, Budget and Control approval is required. But, the present law does not specify how long such lease agreements may cover nor does it convey any sense of the overall policy the Board should follow in approving leases. (8)

(*) Emphasis ours.

Perhaps the most telling discovery of the 1987 Study was finding no system for deciding which permanent improvements are a priority, which buildings are needed most and by what deadline. These serious shortcomings found in this area reveal one of the major motivations for seeking to lease/purchase government office space at costs estimated as much as 60% over and above the cost of State construction and ownership. (9) An inevitable delay of up to four years in some cases, and much longer in others has occurred (State Museum), while internal and external politics determine which State projects will be created first, if ever.

Reform begs to be called upon when one of the most efficient means to construct State business offices is to circumvent the system, even while controversy swirls over whether money paid in exchange for leasing or lease/purchasing real estate is, in fact, regardless of form, debt.

LEASE/PURCHASE AGREEMENTS AS DEBT, A POPULAR DISSENTING VIEW

This Committee agrees with South Carolina Supreme Court Justice A. J. Finney in his dissenting view in Caddell v. Lexington County School District No. 1. et al. Mr. Justice Finney affirmed the decision of the trial court which found "...that the lease agreements between the School District and the Corporation incur a general obligation debt and violate Article X, Section 15, of the South Carolina Constitution".

In a classic victory of form over substance, the South Carolina Supreme Court majority concluded that "...the lease/purchase agreements do not constitute debt as that term is used in Article X, Section 15 ... due to the inclusion of a 'non-appropriation clause', under which the District may decline, without penalty, to renew the annual lease by failing or refusing to appropriate the necessary funds".

In the discussion, the Court majority said "In its historical context, general obligation debt refers to that which is 'ultimately secured by taxes on the property within the political entity'".

"...a leaseback arrangement containing an explicit non-appropriation clause places no such requirement on the political entity. Under the plan here, rental payments are to be included in the District's annual budget. Liability under the leaseback agreement is, at most, contingent: The District has the option of terminating simply by refusing to appropriate money for rent".

But Mr. Justice Finney points to the District's objective of contravening the State's constitutional debt limitation provision in an effort to build a new school, and interprets that "the monetary realities of these lease arrangements conclusively show that the indebtedness is secured in part by the school district's property, which was acquired with its taxing powers".

Mr. Justice Finney asserts that the test for this case should be "whether the indebtedness of the school district is secured in whole or in part by a pledge of its full faith, credit and taxing power, making the leases a general obligation debt for the period of the Project Leases. Should the district invoke the non-appropriation clause and decline to renew the annual Project Leases, the District may be guilty of misappropriating governmental property".

He then contends that the "subject lease agreements are prohibited because they use taxpayers' property as security and involve a pledge of credit. Further, the non-appropriation provision is an attempt to protect the arrangement from constitutional challenges".

He concludes that the "... the lease agreements are a subterfuge to enable the District and the Corporation to evade the District's constitutional debt limitations, which were provided generally to protect the public. Certainly the need to provide facilities determined necessary to educate our youth cannot be overstated. However, no matter how worthy the endeavor, contravening the constitution cannot be justified. THE COLD ECONOMIC REALITIES OF THE RISING COST OF EDUCATION AND REVENUE SHORTFALLS ARE NOT SUFFICIENT REASONS TO OVERLOOK THIS OBVIOUS DEBT LIMITATION VIOLATION. IN MY OPINION, THE CRISES IN THE EDUCATIONAL SYSTEM SHOULD BE REMEDIED BY A CONSTITUTIONAL AMENDMENT OR A VOTE OF THE

PEOPLE. THUS, I WOULD AFFIRM THE DECISION OF THE TRIAL COURT". (*)

It is the view of this Committee that if any political subdivision of the State, including any school district or special purpose district, failed to meet its payments under a lease/purchase arrangement, for whatever reason, it is conceivable that the AAA credit rating of the entire State could be threatened. If political subdivisions of this State choose to circumvent the limitations of their bonded indebtedness, then the Committee recommends that they be required to receive the approval of both houses of the General Assembly prior to entering into any lease/purchase arrangement.

With respect to the controversial "non-appropriation clause", both the Clemson Computer Center and the AG Building involve the sale of certificates of participation. The Clemson Computer Center certificates are rated AAA/AAA and the AG Building certificates are rated AA. (10) Clemson's issue has been insured which effectively guarantees the investors in these certificates of participation that if Clemson exercises the non-appropriation clause privilege the insurance company will continue to make the payments which otherwise would have been made by Clemson. The insurance company obviously sees substantially no risk that Clemson

(*) Emphasis ours.

will exercise this privilege. The AG Building's participation certificates were not insured and, because of the non-appropriation clause, received the AA rating while Clemson's issue received the AAA/AAA rating. These two securities were priced issued on the same day so there should not have been a material change in market conditions between the precise times of pricing and issue. The return to investors is only slightly higher on the AA rated AG Building's certificates than on the AAA/AAA rated Clemson Computer Center certificates. This fact is important because if the State through a Central Building Authority were to issue revenue bonds or participation certificates backed by lease payments, the rating on these instruments would probably be AA/AA because of the inclusion of the non-appropriation clause. (11) The State's general obligation bond rating is AAA/AAA.

PAST LEGISLATION AND DIRECTIVES FOR PROPOSED LEGISLATION

As early as 1981 the legislature realized there were problems in the capital procurement process that needed to be addressed. In the face of sharply increased demands for State office space from a growing government grappling with meeting State needs, the 1985 legislature decided that all real estate transactions must have the approval of the Budget and Control Board. In mid 1986 the Division of General Services recognized the need to improve the State's handling

of transactions involving leasing and lease/purchase features. At that time the Division examined all property management functions and developed an organizational approach which assured proper control of these functions as well as fairness and cost effectiveness in making lease and lease/purchase commitments. 1988 and 1989 appropriations again called for more regulations concerning procedures for determining agency needs.

This examination eventually resulted in reorganization of the Property Management Office within the Division of General Services. The new office combined an appraisal function and the permanent improvement budgeting process with the State's leasing and property acquisition functions. This reorganization enhanced the technical and professional resources available to support real property transactions and provided for effective coordination of such transactions within the permanent improvement budgeting cycle.

The increased focus on property management functions also resulted in a number of innovations designed to assure cost effectiveness and improve control of leasing and lease/purchase transactions. Some of the more important of these are:

Establishing the standards for quantity and quality of space the State leases;

Devising and implementing the use of standard lease forms;

Establishing procedures for rejecting agencies' requests for additional space;,

Directing agencies to locate in public space if available;

Requiring agencies to submit to a multi-year financial plan; and

Requiring the approval of the Joint Bond Review Committee for any major leases. Major leases are defined as a million dollar expenditure within a five year period.

THE MCCONNELL BILL

The McConnell Bill calls for additional regulations. It also addresses the question of adequate office space per person. However, it does not require justification of space needs and does not allow the Division of General Services to reject the request.

The McConnell Bill proposals do not deal with lease renewals other than requiring a sixty (60) day notice prior to renewal.

The Committee believes renewals should be subjected to the same kind of cost analysis that new leases are. In addition analysis ought to be completed a year in advance in order to give the agency the advantage of time in deciding whether the lease should be continued or not. The Committee also believes the language of the proposed McConnell Bill should be strengthened to make it clear that all proposals would be subject to a cost analysis. ANOTHER OF THE AREAS THAT NEEDS TO HAVE REGULATIONS IS THE BID PROCESS. The McConnell Bill takes the language of existing statutes which talks about competitive bidding "where feasible" and changes

it to "competitive proposals", i.e. competitive proposals are required.

The proposed legislation of Senator McConnell is a mighty step in the right direction, but we have noted in some instances it does not go far enough. While it does attempt to establish some sort of standardization and create a more open leasing system, THE COMMITTEE RECOGNIZES ONE ASPECT OF THE BILL WHICH MUST GO ONE STEP FURTHER: Requiring ALL lease/purchase agreements of the State and its political subdivisions, including school districts and special purpose districts, to have the prior approval of the GENERAL ASSEMBLY. This extension of the approval process would provide much needed control over the apparent inpeding proliferation of lease/purchase arrangements throughout the State. This additional provision to the proposed legislation is critical and urgently needed to prevent substantial and irrevocable harm to the credit rating of the State of South Carolina.

The Committee also believes another portion of the bill that needs strengthening is the one dealing with five year plans. The more it is strengthened the better able the State will be to get a handle on its future needs.

The Committee believes the Division of General Services can provide strong control of leasing functions provided it is given the statutory authority to carry out a mission of assuring fairness, competition, and cost effectiveness with respect to State activities.

The Committee strongly supports the McConnel legislation in general, and recommends that the regulations to be promulgated thereunder be detailed, precise and have "teeth" with adverse consequences for offenders.

The Committee is in agreement that reforms already underway within the Division of General Services are well conceived steps in the right direction for operating a more businesslike State government, where efficiency, cost control, and short as well as long term planning and forecasting are viewed as critical to serving the needs of a growing South Carolina. However, the Committee believes that IF THE DIVISION OF GENERAL SERVICES IS GOING TO MOVE FROM A SERVICE AGENCY THAT HELPS STATE AGENCIES MERELY TO FIND SPACE, TO A MONITORING AGENCY WHICH OVERSEES COST, THERE HAVE GOT TO BE SOME REAL REGULATIONS IN PLACE TO ALLOW THE DIVISION OF GENERAL SERVICES TO FULFILL ITS NEW FUNCTION AND RESPONSIBILITIES.

CONSIDERATIONS OF A FACILITIES ADMINISTRATOR AND A STATE BUILDING AUTHORITY

After listening to testimony and researching the issue, it is the belief of this Committee that the Division of General Services has done an admirable job in the past couple of years to significantly improve the process that has developed over the last decade or so. The current process, while it could be improved and expanded and no doubt will be, probably would work effectively if left alone and the capable

personnel of the Division of General Services were allowed to perform their duties and responsibilities in this area without political interference.

Even though the Division of General Services has made substantial improvement in the past two years, there is still a perception by many, supported in some instances, that would indicate the current system is still not sufficient to prevent abuses in the leasing process. It also appears that THE MOST NOTABLE EXAMPLES ARISE WHEN THE AGENCY OR DEPARTMENT HEADS, OR DESIGNATED REPRESENTATIVES, ATTEMPT TO SUBVERT THE PROCESS AND DEAL DIRECTLY WITH THE OWNERS OR AGENTS OF SPECIFIC PROPERTIES. IN ADDITION TO THIS DILEMMA IS THE AGE-OLD PROBLEM OF POLITICS INJECTED BY THE POLITICAL SUPPORTERS OF THE SPECIFIC AGENCY OR DEPARTMENT INVOLVED.

It would appear that since the process is currently being circumvented, that the only way to effect change is to alter the method of doing business in this area.

Although the current law and the proposed regulations do require the Division of General Services to handle State leases, with the Budget and Control Board as a final appeal and determinative body, it seems that the taxpayers of South Carolina could be better served by a specific entity or office within the Division of General Services with the sole responsibility of reviewing, negotiating, selecting, bidding and studying the lease needs of agencies and departments of State government, as well as setting policy in the area.

This specific entity or office within the Division of General Services, which we would propose designating the Office of Facilities Administration ("OFA"), should be permitted to hire from, contract with, and draw on the vast pool of private sector experience and expertise in the leasing area to formulate policy, procedures and practices that would insure that South Carolina taxpayers are receiving the very best available for tax dollars expended on private space needed to accommodate the needs of State government. In addition, the OFA would make determinations as to when it would be more feasible to build and own space rather than to continue to lease.

It makes sense for the State to own its own buildings. The establishment of a State Building Authority would allow the State to utilize the current flow of rental funds from State buildings to support the issuance of revenue bonds and participation certificates as sources of funds for the construction and operation of a large part of the needs of State government. This apparently is a novel idea in South Carolina, whose time has come. It is in use in other states and was described in detail in the apparently neglected 1987 Study. If the Authority ever has more space available than the State can fill, it could, conceivably, lease this space to the private sector.

This Committee believes that neither the establishment of an OFA nor the creation of a Central Building Authority

will require any significant increase in personnel or facilities within the Division of General Services.

With all the obvious problems stemming from allegations of profiteering, though often politically motivated, but allegations nonetheless, there has been created an unwholesome atmosphere which surrounds the State's management of its facilities. It is obligatory that the State's vast leasing and property management program, which deals of necessity with the State's revenues, not only be managed in the most frugal and efficient fashion available, but also be administered honestly and in all instances in keeping with the highest and most stringent ethical practices and standards. However, in order for this unwholesome atmosphere to be dissipated, it is essential that this program be <u>perceived</u> in this fashion. This Committee believes that the Division of General Services should aggressively accentuate in the public media the positive aspects of its organization and the progress it is making.

HISTORIC PRESERVATIONS: IS IT A LEGITIMATE FUNCTION OF THE STATE GOVERNMENT TO UNDERWRITE THE SUCCESS OF REAL ESTATE TRANSACTIONS:

Two questions should be considered when answering this issue:

1. Does the fact that a particular real estate transaction aid in the revitalization of a city or other area have relevance to the legitimacy of this underwriting function?

2. Does the State have a responsibility to protect and use important cultural facilities which it has under its control or which it may acquire? If so, what additional cost, if any, is justified in the State's pursuit of preservation as a method of enhancing the quality of life of its citizens?

The State government should further the "public interest" in its real estate transactions. The "public interest" has many aspects. Obviously, conserving tax dollars is a very important public interest. However, historic preservation of culturally significant buildings and downtown revitalization are also within the "public interest" and should be taken into consideration as factors when analyzing the advisability of a real estate transaction of the State.

Clearly, historic preservation was a factor in the sale/lease-back projects involving the State Museum and the Robert Mills Building. And it is possible that these intangible public interests could constitute a "State Subsidy" whereby the tangible benefit exceeds the cost. It is also possible, though not likely, to assume that the AT & T project furthered a legitimate public interest by aiding in the revitalization of the Columbia area.

Policy recommendations should include a recognition of other legitimate State functions in the leasing process such as historic preservation.

Whenever the State wishes to further public interests other than obtaining cost effective space, the purpose should be stated as a State objective prior to entering into the

lease and should be analyzed as a separate component of the lease project.

Once the other public objective is stated, the State should explore means of achieving objectives which are as cost effective as possible. For example, if the State objective is historic preservation, the following questions should be asked:

a) Is the building of such historic significance that it would be renovated regardless of cost or is the historic significance of a more limited nature?

b) Is there a private means of achieving the historic preservation?

c) Could the property be sold to a private entity subject to restrictive covenants requiring renovation and prohibiting the destruction of its historic character?

d) Is the lease/ purchase of the project the most cost effective means of achieving both the need for space and the historic preservation?

The cost of the project requiring historic preservation should be compared to alternative lease arrangements which do not involve historic preservation in order to derive the cost attributed to historic preservation. Once the actual cost of the historic preservation aspect of the project is isolated, the State will be better able to develop creative solutions to further both the State objectives in the most cost effective manner.

It is the conclusion of this Committee that renovating historical structures specifically for office space is not

necessarily "getting two for one" in value. The costs of renovation often exceed building new from the ground up.

Other State interests beyond providing cost effective office space for State agencies are often furthered by State leasing arrangements. However, whenever the State departs from a strict cost analysis of housing needs, these additional State objectives should not be used to provide justification for otherwise inefficient use of State funds. When a lease project is analyzed, the cost of any alternative methods of achieving such legitimate State interests should be compared to the costs associated with the proposed lease project.

HOW CAN IT BE IN THE BEST INTEREST OF THE STATE FOR ITS AGENCIES TO VACATE STATE OWNED SPACE AND MOVE INTO MORE EXPENSIVE LEASED SPACE?

The evidence shows all State owned space that was vacated by some agencies moving to new space is now fully occupied. But when a selected group of leases over the past four years are examined it is found that there has been a 54% growth in agency space, from 320,000 square feet to 494,000 square feet. Evidence also shows that there has been fairly substantial documentation and justification for an agency moving into new space. Reasons for moving into new space include the need for more space, the need to consolidate functions, or consolidate with another agency, the need to

improve location and access, and generally to provide for the dynamics of a growing and evolving State government.

Whether or not all the agency moves in the past are justifiable is not within the scope of this Committee's assignment. Since all the State owned space is occupied and the State is not willing to add more space, the only answer seems to be to lease space or obtain space through lease/purchasing.

THERE IS A LACK OF DEFINED STATE POLICY REGARDING THE OWNERSHIP OF STATE FACILITIES AND A LACK OF A POLICY THAT ADDRESSES THE SPACE FINANCING TECHNIQUES THAT OUGHT TO BE EMPLOYED IN THE EVENT THE STATE CANNOT FULFILL THE AGENCIES' REQUESTS FROM ITS OWNED FACILITIES. There is no legislation addressing to whom the agency is accountable for deciding staff size. This is important since space, afterall, is a follow-up assumption to staff size. (13)

THE ADVANTAGES AND DISADVANTAGES OF LEASE VS. PURCHASE

It seems appropriate to here first describe what appears to have been an educational process at the Budget and Control Board as lease/purchasing has evolved in South Carolina. This Committee views the State Museum and the Robert Mills Building lease/purchase financing arrangements as the first stage in this evolution. Following the failure of the State to pursue other options, these Tier I lease/purchase arrangements were brought to the State by developers,

who, racing the clock to benefit from historic preservation investment tax credits that would expire after December 31, 1984, convinced the State that these were the best financing techniques available to restore these two State owned buildings for historic and office space purposes. The economic benefits of the 25% federal investment tax credit ("ITC") would be passed through to the State by the investors, thus achieving for it indirectly a benefit for which the State was not directly eligible. This Tier I lease/purchase arrangement was "deal driven". The developers had found a way to do a real estate tax deal in the twilight of the tax law prior to the relevant effective date of the repeal provision of the Tax Reform Act of 1984. Without the ITC, neither of these deals would have worked. However, the ITC indirect benefit to the State may not have been enough to offset the interest rates built into the lease payments necessary to service the investor debt incurred in these two transactions.

Then came the Tier II lease/purchase arrangements under which the State entered into a financing agreement with a developer, similar in all but one critically important feature to the Tier I arrangements. The Tier II arrangements involved the Clemson University Computer Center Project ("Clemson Computer Center") and the South Carolina Adjutant General Building Project ("AG Building"). Here the developer was involved in a transaction with the State where financing

was obtained in a tax exempt revenue bond type financing. It appears that the developer may have educated the Budget and Control Board by showing them how tax exempt financing could be used to finance both of these facilities in a lease/purchase transaction. The middleman developer remained after the concept was apparently introduced and explained. However, the result was that a bond issue (called "participation certificates") was used to finance both the Clemson Computer Center and the AG Building with leases assigned to support the retirement of the debt. Both of these leases contain the standard "non-appropriation clause", yet the Clemson Computer Center bond issue is rated AAA/AAA, due to bond insurance, and the AG Building bond issue is rated AA without bond insurance. In both instances it is clear that the financial community did not take seriously the non-appropriation clause. (14)

Finally, came the Tier III lease/purchase arrangements. Apparently, now having been introduced to lease/purchasing by developers in the Tier I arrangements, then educated by the developer in tax exempt financing for the lease/purchase used in the Tier II arrangements, the Budget and Control Board was sufficiently knowledgeable in this technique to pursue it on its own without the middleman developer. It is these Tier III arrangements that must not be confused with Tier I and Tier II arrangements, both of which involve middlemen

developers, and the first of which involves more expensive conventional financing.

The Tier III arrangements essentially involve State ownership of the property financed with revenue bond type debt. An instrument called a participation certificate is issued the "bondholder" but in all but name it is a bond. It was this Tier III method of lease/purchase financing that was proposed for the new CCI facility in Lee County. Essentially, a prison authority (e.g. a building authority) was to be established to build and own the prison. No middleman developer would be involved although there may have been a third party who would manage it. The prison authority would put out the building contract for bids under the State's standard low bid process. The prison would be constructed and leased to the appropriate State agency -the Department of Corrections- with the standard "non-appropriations" clause in the lease. The prison authority would issue tax exempt certificates of participation which would carry coupons at the same rate or approximately the same rate, as a South Carolina Revenue Bond-about 25 basis points above the South Carolina General Obligation Bond ("GO Bond") yield for a comparable maturity. (15) This "revenue bond type financing" would give the State, when coupled with the absence of a middleman, a facility at a cost only slightly more expensive than if it had been financed with GO Bonds.

The Lexington I School District proposed lease/purchase financing of its new school facility would work in this same fashion.

To the extent this Committee's pronouncements on lease/purchase arrangements have "tarred all of them with the same brush" it has been unintentional.

The point the Committee makes with respect to Tier III lease/purchase financing is that it wants to be certain that the Budget and Control Board, and the governing bodies of the State's political subdivisions, recognize it for what it is - debt. It is debt in the eyes of the investor and financial communities as the "non-appropriation" clause is viewed as without substantive effect. It may even be debt in the constitutional sense as South Carolina Supreme Court Justice A. J. Finney concluded in his dissenting view in Caddell v. Lexington County School District No. 1 et al. In any event when the Budget and Control Board and the governing bodies of the State's political subdivisions are making a determination of how much "debt" can be serviced by the State or its political subdivisions, all obligations that must be paid or repaid-lease, lease/purchase, revenue bond, participation certificates, and GO Bonds-should be included in the total indebtedness. It would be constructive if the news media using its reporting process as an educational tool, made the real components of the State's and its political subdivisions' debt clear to the public. It really

is an anachronism to engage in the niceties of distinguishing constitutional debt from other obligations which must be repaid when the financial community views them all as indebtedness.

The only real differences between the State's outright purchase of a facility, whether financed by GO Bonds, revenue bonds or Tier III Lease/Purchase arrangements, and the Tier I and Tier II lease/purchase of a facility are the cost of borrowed funds and the absence of a middleman.

With reference to the Mt. Vernon Mill (State Museum) and the Robert Mills Building it has already been noted that both renovation projects were essentially "deal driven" by private developers who were invited to bid on the renovation projects when no State funds were available. Had private developers not taken an interest in the projects they would very likely not have been done.

From a strict economic perspective it is clear the State should always attempt to purchase its own structures. When a discounted cash model was used to analyze the State's obligations under the Tier I lease/purchase arrangements employed in these two projects, it was found that the State was paying considerably more than it would have had the State built the facilities and issued GO Bonds to finance them. These calculations showed that the State paid a substantial premium in present value dollars for the privilege of using Tier I lease/purchase arrangements to assure these projects'

timely completions. If the State could have funded these two projects within the debt limit of the State there would have been no justification for the Tier I lease/purchase arrangements. In general it would be very difficult to justify any lease/purchase arrangement involving a private developer (a Tier I or Tier II arrangement) in which the State would enter.

A true leasing arrangement may be justified if the lease is for a short term or if it is for a small amount of money. However, short term true leases often become long term leases because of renewal. When the State's needs require a large capital commitment or a long term space requirement, the State would always be financially better off to own its own facilities rather than to lease them or to acquire them under Tier I and Tier II Lease/Purchase arrangements.

THE NECESSITY/FEASIBILITY OF DEVELOPING A STATE OFFICE ALLOCATION PLAN

At this time there is no current space plan or forecasting study for State office buildings, and there has not been one since 1986. Meaningful guidelines using an official space index should be established and enforced. It is the recommendation of this Committee that a Space or Office Allocation Plan be developed immediately to forecast space needs for three to five years. Prior forecasts should be updated annually. Comparable agencies serving complimentary or interacting functions should be grouped

together to share locations, facilities. and equipment. Building technology and lay-out, designed to achieve the most efficient use of space, equipment, technology, service and money, should be studied and recommendations made. For example, rectangular buildings are generally less costly to build and yield more private offices; square buildings offer greater density and accommodate more work stations; sixty (60) feet from core to exterior wall is an ideal dimension for planning flexibility.

Rather than have agencies request space according to their own desires and perceived needs, a top-down approach should be used. After agency directors have been asked to justify space needs in quantifiable terms, they would be allocated a specific amount of space by the OFA from which to operate agency functions. The OFA may grant the agency more or less space than requested in a location that may or may not be the same as requested. The decision of the OFA would be final, subject only to appeal to the Budget and Control Board.

South Carolina's monument buildings within the Capitol Complex are currently complete, impressive and large enough to memorialize the seat of State government. It is clear that it is cheaper for the State to build and maintain its own property. Since it can borrow money at less than any private developer (at least 3% to 4% less), it cannot only build cheaper but the working capital necessary to fund building operations and maintenance is less expensive. The

State also has more clout than any private developer and should pay less for insurance and utilities. There obviously would be no property taxes, and maintenance would be performed by State employees. These savings keep the costs of owning and maintaining well below what any private developer can offer. If the State builds through a Central Building Authority it pays only the amount of rent necessary to service the debt on the building.

While it is not within the scope of this Committee to review the personal property, equipment, and furnishings acquired by agencies, it is clear that with careful planning the costs of those purchases can be better controlled. If a building were designed and furnished using a well coordinated color scheme and style of furniture, for example, three or four complimentary colors that ran throughout an entire building and one wood grain and one style of furniture, then furnishings could be moved among floors and offices without the extra expense of refurnishing and redecorating.

Any further buildings constructed by the State should have as their first priority a utilitarian design which would include the capability to be expanded. This would very likely require that the State look beyond the city limits of Columbia to develop a campus type environment where buildings could be located on land with ample space to expand and could be functionally designed to meet the State's growing needs.

Those agencies that do not need to be located in the Capitol area should gradually be relocated to more appropriate and more economical locations. Agencies both in Columbia and satellite cities throughout the State should be grouped to the extent that economies may be obtained through the inter-relationship of their functions. Except to the extent that OFA may determine after consideration of all of the variables inherent in a cost and function analysis of location, that there is a clear case for location near the Capitol area, it should be strongly discouraged. Competition for space in downtown Columbia, where the State is by far the single most prevalent user of office space, drives up the costs of that space. Even to the extent the State builds its own buildings in downtown Columbia it drives up land costs, a component of space cost. THEREFORE, ANY AGENCY FUNCTION WHICH CAN BE EFFECTIVELY HANDLED OUTSIDE DOWNTOWN COLUMBIA, SUCH AS THE HEALTH RELATED SERVICES FACILITIES NOW BEING DEVELOPED IN THE NORTH TOWER AREA, SHOULD BE.

CONCLUSION

It is the conclusion of this Committee that in the last year, if not the last six months, a tremendous advancement in the understanding of State leasing practices has evolved. Due to the public discussion, legislative study and media attention, the State is beginning to realize that leasing office space is more expensive in every instance, with the

exception of very short term leases, than if the State were to build and maintain its own buildings.

It is also the conclusion of this Committee that all lease/purchases are not created equal - that as the lease/purchase process became more popular in South Carolina as an alternative to providing office space it also became more sophisticated. (Tiers I, II, and III)

It also is apparent to this Committee that the Budget and Control Board and the Division of General Services have come a long way down the learning curve quite recently. Ironically, it is a study by the Budget and Control Board and the Joint Bond Review Committee that is the key to understanding here. It is the conclusion of this Committee that if the Budget and Control Board, members of the Legislature, and key State personnel had thoroughly digested the landmark, but apparently largely unnoticed, or if noticed, unheralded, STUDY OF LEASE/PURCHASE AND OTHER PRIVATE FUNDING MECHANISMS FOR CAPITAL IMPROVEMENTS (January, 1987) what are perceived to be current problems, could have been identified earlier and now be well on their way to being corrected. Had in 1985 the then Budget and Control Board and the then Department of General Services known certain data and understood certain concepts discussed in the 1987 Study, such as the concept of a central building authority, the AT & T Building would very likely be the flagship today of a South Carolina Central Building Authority. The irony of the AT & T developers buying State property from the University

of South Carolina, or an instrumentality related to it, as the case may have been, simply to tear down the improvements and build a new building to lease back to the State cannot go unnoticed. The State could have kept the property that it already owned, albeit indirectly through the University, and built the AT & T Building at a substantial savings due to its bargain cost of funds as opposed to that available to the private developers.

Many of our conclusions, reached independently after much study are similar, if not identical in some cases, to those recommendations of the 1987 Study by the Budget and Control Board and the Joint Bond Review Committee. We feel that the State, through its staff and citizens' committee, having inadvertently done much the same lease study twice, should pay special heed to the advantages of having two reports that confirm many of the same conclusions.

ENDNOTES

(1) Clemson University (Computer Center) Lease/Purchase Participation Certificates Due 2007 came at Par on December 1, 1986 with the 2007 maturity to yield 6.90%. South Carolina Adjutant General Building Lease/Purchase Participation Certificates Due 2007 came at Par on December 1, 1986 with the 2007 maturity to yield 7.00%. The difference in yield was only 10 basis points between the insured AAA/AAA (Moody's/Standard & Poor's) Clemson Computer Center Participation Certificates and the AA (Standard & Poor's only) uninsured AG Building Participation Certificates. These are now trading at the same yield to maturity. See endnote 2.

(2) On December 23, 1988 the following general information quotations were received by telephone from Smith Barney, Harris Upham & Co., Incorporated:

South Carolina General Obligation Bonds Due 2007 AAA/AAA (a)
7.35% Yield to Maturity

South Carolina Public Service Authority (Santee Cooper) Revenue Bonds Due 2006 A1/A+
7.60% Yield to Maturity

Clemson University (Computer Center) Lease/Purchase Participation Certificates Due 2007 AAA/AAA
7.60% Yield to Maturity

South Carolina Adjutant General Building Project Lease/Purchase Participation Certificates Due 2007 AA (b)
7.60% Yield to Maturity

State of Florida, Department of General Services, Division of Facilities Management (Florida Facilities Pool Revenue Bonds) Due 2006 A1/A+
7.70% Yield to Maturity

(a) Moody's/Standard & Poor
(b) Standard & Poor's only

These yield comparisons indicate that Participation Certificates issued in lease/purchase arrangements in South Carolina and South Carolina Public Service Authority (Santee Cooper) Revenue Bonds all of nearly comparable maturities and quality may trade at only 25 basis points higher than a South Carolina General Obligation Bond.

In the December 23, 1988 edition of The Wall Street Journal a yield comparison of General Obligation Bonds and Revenue Bonds based on the Merrill Lynch Bond Indexes, priced as of midafternoon Eastern time, December 22, 1988, shows the following:

New tax-exempts

20-yr G.O. (AA) 7.40% Yield to Maturity

30-yr Revenue (A) 7.80% Yield to Maturity

These yield comparisons indicate that even a lesser grade revenue bond with a 10 year longer maturity may trade only 40 basis points higher on a yield to maturity basis than a G.O. bond of shorter maturity and higher grade.

(3) An old Chinese proverb declares that "the beginning of wisdom is in calling something by its right name".

(4) An expansion of the concept of a "Leasing Czar".

(5) Using the terminology of this report, the 1987 study would be referring to Tier I and Tier II Lease/Purchase Arrangements.

(6) 1987 Study, page 5.

(7) Under the 1988 Caddell decision the South Carolina Supreme Court has specifically excluded lease/purchase obligations as constitutional debt.

(8) 1987 Study, pages 6 and 7.

(9) Using the terminology in this Report, the 1987 Study would be referring to Tier I and Tier II Lease/Purchase Arrangements.

(10) See Endnote 1.

(11) See Endnote 2.

(12) California, Florida and Michigan have had substantial and favorable experience in the use of building authorities as mechanism for owning their own facilities.

(13) While it is beyond the scope of this Committee's inquiry, we feel we should emphasize that we believe it is clear that space is a follow-on function of people. There must be as much justification for an expansion of people as there is for creation of space. The efficiency of an agency must be audited and determined before a valid justification for more space can be made. This Committee understands that when additional personnel are requested in a budget, their number and cost are reflected in bold italics. We believe that a space cost component for additional personnel should be highlighted in like manner in the budget request.

(14) See Endnote 1.

(15) See Endnote 2.